



**Office of Audit Services**  
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June 16, 2006

#### **AGENDA ITEM 4**

#### **TO: MEMBERS OF THE FINANCE COMMITTEE**

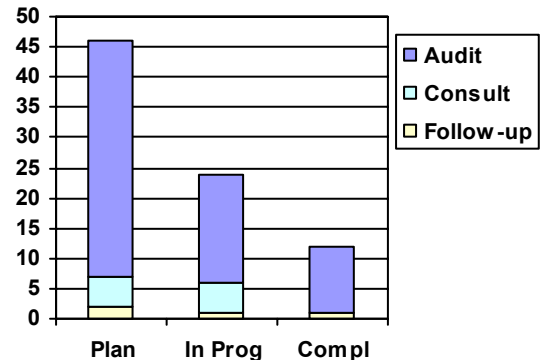
- I. SUBJECT:** Quarterly Status Report
- II. PROGRAM:** Audit Services
- III. RECOMMENDATION:** Information only
- IV. SUMMARY:**

In accordance with the Finance Committee's Audit Resolution Policy and Procedures, the Office of Audit Services presents its Quarterly Status Report of audit activity. The following provides the status of audits and special projects as of March 31, 2006.

#### **1. Status of projects and activities in the Fiscal Year 2005 / 2006 Board approved annual Audit Plan**

- A. Internal Audits – Internal audit projects and consulting assignments focus on compliance, and the effectiveness and efficiency of CalPERS operations, systems, policies, and procedures. Detail on these projects is provided on Attachment 1A.

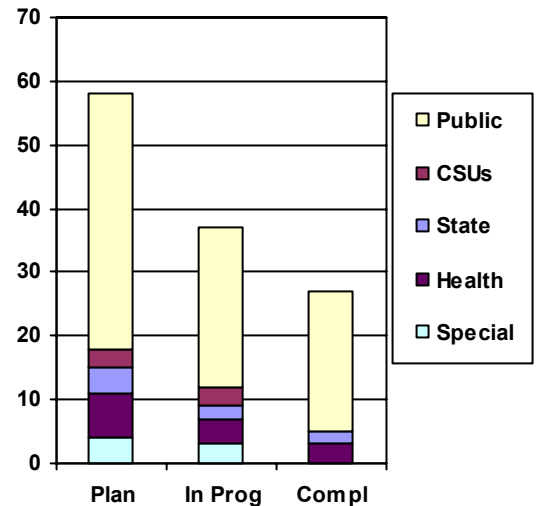
2005/06 Board Approved Audit Plan	Plan	In Progress	Complete
Audit Projects	39	18	11 <sup>A</sup>
Consulting Projects	5	5	0
Audit Follow-up	2	1	1



A – Includes projects that started in prior fiscal year as outlined in Attachment 1A.

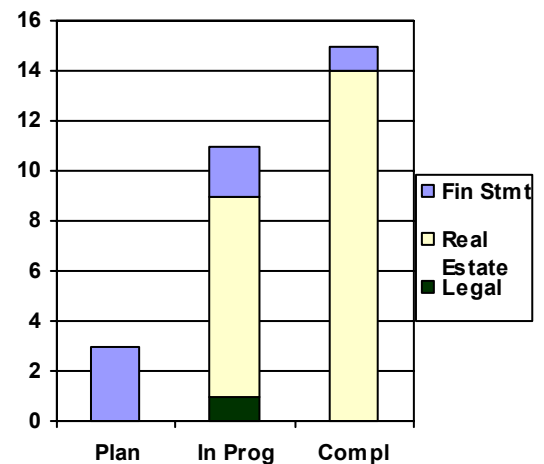
B. Field Audits and Reviews— Field audits and reviews include compliance reviews of employer entities belonging to the System, audits of Health Maintenance Organizations contracting with the System, compliance audits of health care third-party administrators, and audits of external providers of investment-related services. Detail on these projects is provided on Attachment 1B.

2005/06 Board Approved Audit Plan	Plan	In Progress	Complete
Public Agency Reviews	40	25	22 <sup>A</sup>
California State Universities Reviews	3	3	0
State Agency Reviews	4	2	2
Health Plan Audits	7	4	3 <sup>A</sup>
Special Projects	4	3	0



C. Contract Audits – Contract audits include audit work performed by external auditors. The number of real estate audits is determined over the course of the fiscal year. Detail on these projects is provided on Attachment 1C.

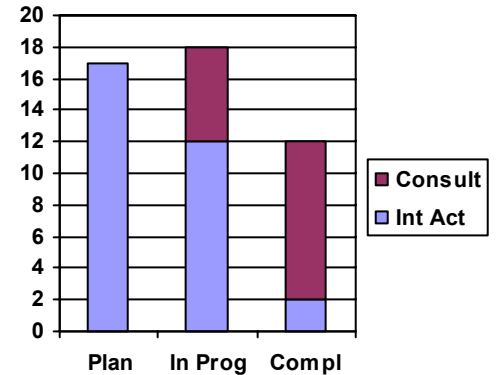
2005/06 Board Approved Contract Auditor	Plan	In Progress	Complete
Financial Statement Audits	3	2	1
Real Estate Audits	As requested	8	14
Legal Fee Audits	As requested	1	0



A- Includes projects started in prior fiscal year as outlined in Attachment 1B.

D. Management Consulting Projects - In addition to the specific projects in the approved Audit Plan, during the year the Office of Audit Services responds to subsequent requests from the Board of Administration, Executive Management, and program divisions for audit and consulting projects. The approved Audit Plan includes an allocation of hours for these projects. Detail on these projects is provided in Attachment 1D.

Management Consulting Projects	Plan	In Progress	Complete
Management Consulting Projects	As requested	6	10
Office of Audit Services Internal Activities	17	12	2

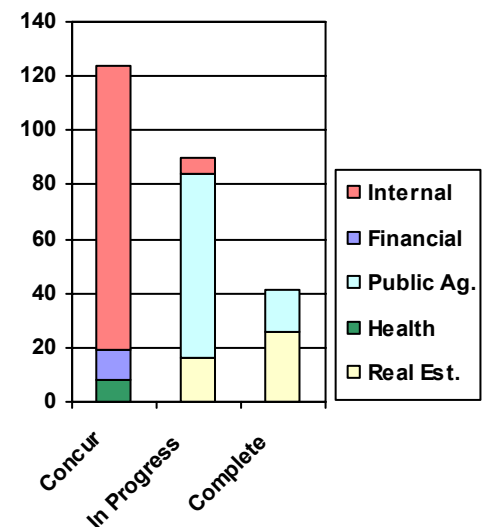


## 2. Findings / issues resulting from auditing work

A status of *Concur* indicates management has agreed with the finding and plans corrective action. *In Progress* indicates management is taking corrective action. *Complete* status indicates satisfactory resolution of the finding. *Unresolved* status indicates management does not agree with the finding or recommendation or has not taken adequate action; in such a case, the finding is referred to executive management for resolution.

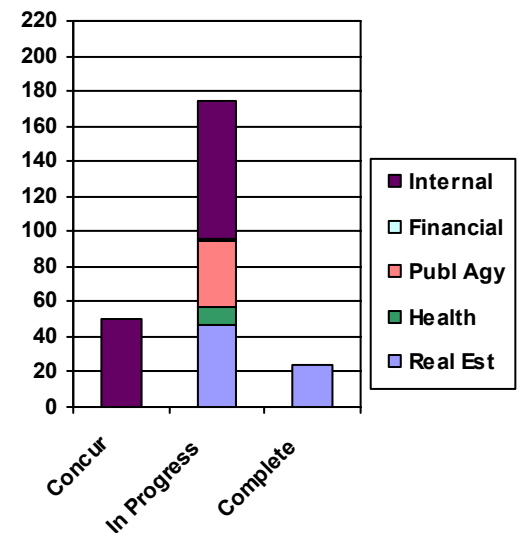
A. Findings / issues resulting from current year projects.

Activity	Concur	In Progress	Complete	Unresolved
Internal Audits	105	6	0	0
Financial/External Audits	11	0	0	0
Public Agency Reviews	0	68	15	0
Health Plan Audits	8	0	0	0
Real Estate Audits	0	16	26	0



B. Findings / issues resulting from prior years' projects.

Activity	Concur	In Progress	Complete	Unresolved
Internal Audits	50	78	0	0
Financial/External Audits	0	1	0	0
Public Agency Reviews	0	38	0	0
Health Plan Audits	0	10	0	0
Real Estate Audits	0	48	23	0



3. Findings / Issues

During the first three quarters of Fiscal Year 2005/06, we completed 24 reviews of contracting entities. The most frequently reported issues were incorrect reporting of compensation, not enrolling eligible part-time employees, and payroll reporting errors. The following table is a summary of the findings included in the reports issued during the first three quarters of Fiscal Year 2005/06.

Type of Finding – FY 2005/06	Number of Findings
Compensation	18
Enrollment	16
Payroll reporting errors	13
Contributions/payroll information not reported timely	10
Unused sick leave	9
Reinstatement of retired annuitants	7
Independent contractors	3
Publicly available salary schedule not available	3
Industrial disability not made timely	2
Payrate reporting error	2

### Internal Audits

During the first three quarters of Fiscal Year 2005/06, we completed 11 internal audits focusing on enterprise risk to the organization. The areas of primary emphasis included financial accountability and internal control compliance, contracting and purchasing activities, Medicare transfer eligibility, information technology controls, benefit adjustments, and securities lending collateral management. Key issues reported included the need for improved compliance with State Administrative Manual internal control requirements, controls over the building manager's cash activities, contracting and purchasing activities, issues related to information system access, benefit adjustments, and notification and follow-up to members of their eligibility for Medicare. Detail on these issues will be reported on our June 30, 2006 Quarterly and Year-End Status Report.

### Acceptance of Risk – Internal Audits

In our Quarterly Status Report as of December 31, 2005, we reported on management's acceptance of risk of two findings related to health care fund cash flow. The issues relate to processes under the management of the Health Benefits Branch involving a mismatch between the time outgoing payments from CalPERS to health plans are due compared with incoming health premium payments from contracting agencies. Health Benefits Branch is further analyzing alternatives for resolution of the issue and will seek Executive approval for the recommended alternative. We will report these findings as in progress until resolved.

### Management Consulting Projects

The Office of Audit Services completed ten requests for management consulting projects in the first three quarters of the fiscal year. Major projects included reconciliation assistance to Fiscal Services' Investment Accounting area, a review of the fixed income management system trading compliance, Board election observation, assistance with the accountability for performance initiative, and a special review of certain benefit payments.

### Audit Follow-Up

Consistent with the Audit Resolution Policy and Procedures that took effect July 2005, the Office of Audit Services worked with management to either resolve or develop corrective action plans for 86 audit issues more than one year old, with the result of resolution of a number of older outstanding issues. We will report on the status of all remaining audit issues, including

management's corrective action target dates, on our June 30, 2006 Quarterly and Year-End status report.

#### Health Plan Audits

We completed three audits of health plan contract compliance during the first three quarters of the fiscal year. These audits addressed HMO, pharmacy, and long-term care areas. The main issues identified in these audits include improved reporting of data to CalPERS and improved eligibility tracking. Detail on these findings will be included in our June 30, 2006 Quarterly and Year-End status report.

#### Financial Statement Audits

The external financial statement auditor, Deloitte and Touche, completed its audit of CalPERS' financial statements as of June 30, 2005, and presented an unqualified opinion at the November 2005 Finance Committee meeting. Deloitte presented a draft management letter summarizing all its findings and recommendations related to the financial statement audit at the February 2006 Finance Committee meeting. The issues presented by the auditor include lack of accounting reconciliations, lack of adequate accounting controls and processes for summarizing, recording, and disclosing accounting data, and certain information security concerns.

#### Real Estate Audits

The external real estate auditors completed 14 audits in the first three quarters of Fiscal Year 2005/06. The most frequently reported issues, as in Fiscal Year 2004/05, continue to address insurance requirements, property condition, record-keeping, various fee calculations, and competitive bidding. A summary of real estate audits is found on Attachment 1C – Real Estate, included in this agenda item.

#### Legal Fee Audits

Each year, CalPERS selects one or more projects or litigation matters conducted by outside counsel to be audited by an external legal audit firm. One such engagement is currently in progress. The Legal Office plans to present the final report as an information item to the Finance Committee upon completion.

**V. STRATEGIC PLAN:**

This item is not a specific product of the strategic plan, but is required by the Finance Committee's Audit Resolution Policy and Procedures and the Office of Audit Services Charter.

**VI. RISKS/COST:**

This is an information item and does not result in any risks/costs. Staff is available to answer any questions that the Finance Committee may have.

*Original Signed by Larry Jensen*

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Larry Jensen, Chief  
Office of Audit Services

*Original Signed by Peter Mixon*

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Peter H. Mixon  
General Counsel